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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969

Nos. 914, 915, 916, 917, 920, 921, 1038, 1057

NEW HAVEN INCLUSION CASES

On Appeals from the United States District Court for the Southern District of New York and on Writs of Certiorari to the United States Court of Appeals for the Second Circuit Before Judgment

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BRIEF FOR APPELLEE, STATE OF NEW YORK

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BRIEF FOR APPELLEE, STATE OF NEW YORK

Statement

This brief of appellee, State of New York, will deal solely with the question whether the Interstate Commerce Commission ("Commission") and the two reviewing courts were correct in holding that the right of The New York, New Haven and Hartford Railroad Company ("New Haven") to free use of Grand Central Terminal in connection with the performance of deficit passenger operations had no value and therefore should not be reflected in determining the price to be paid by Penn Central Transportation Company ("Penn Central") for the New Haven's assets, based on an assumed liquidation. This

question, with some differences in wording by the several appellants, is presented as No. 1(c) in the brief of Manufacturers Hanover Trust Company ("Manufacturers"), No. 9 in the brief of The Chase Manhattan Bank, N.A. ("Chase"), and No. 10 in the brief of The New York, New Haven and Hartford Railroad Company First Mortgage 4% Bondholders Committee ("Committee").

Under 1907 and 1913 agreements between the New Haven and Central, revenues from hotels and office buildings in the Grand Central Terminal complex which were jointly financed and developed, as well as those from the Grand Central Terminal ("G. C. T.") itself, would go into the so-called Terminal Account and be used to help defray or offset the terminal operating expenses, taxes and interest on capital expenditures. Prior to 1964, the total income was inadequate to cover such expenses and the difference was made up by the New Haven and Central on the basis of their relative proportion of total car and locomotive entrances into the Terminal, the New Haven's share averaging about 41 percent.

During the years 1964-1968, the income from the Terminal, office buildings and hotels exceeded the total expenses. The Commission projected the future annual income from the G. C. T. properties at $18,400,000 and the annual expenses at $13,850,000, leaving an excess of $4,550,000. The New Haven was held to be entitled to half of this excess which, capitalized at 8 percent, resulted in a total of $28,887,000, which was included in determining the purchase price. (334 I. C. C. at 39, App. p. 126a) The two reviewing courts agreed with this valuation. Manufacturers (Br., pp. 56-62), Chase (Br., pp. 72-81), and the Committee (Br., pp. 118-130) all contend that, in addition, the purchase price should have been increased by $70,000,000, based on capitalizing at 8 percent the $5,600,000 of income from the Terminal, office buildings and hotels which, they claim, was used to offset the New Haven's share of the Terminal expenses, taxes and inter-

est on capital expenditures. In substance, they contend the estate is entitled to the capitalized value of the New Haven's share of the total income from all of the G. C. T. properties *before* expenses. The Commission and the two reviewing courts were clearly correct in rejecting this contention of the appellants.

Argument

The value placed by the Commission on the New Haven's interest in the G. C. T. properties is obviously quite generous, in view of the initial doubts of the Commission and the New Haven Trustees that *any* interest would survive the discontinuance of passenger service by the New Haven. (331 I. C. C. at 681, App. p. 39a)

Since the Commission and the reviewing courts held that New Haven's right to free use was worthless, there was no need to examine appellants' claim that the amount of income from the office buildings and hotels used to offset New Haven's share of the Terminal operating expenses was $5.6 million annually. The total amount of expenses going through the Terminal Account was about $13.6 million annually (334 I. C. C. at 33, App. p. 120a), of which the New Haven's 41-percent share amounted to $5.6 million. However, only about $9.5 million of the total expenses in the Terminal Account represented operating expenses (334 I. C. C. at 33, App. p. 120a), with the balance being interest on capital expenditures, taxes, etc. (Ex. No. PC-1, R. Doc. No. 57), which obviously must be deducted before arriving at a net figure. Moreover, the $9.5 million of Terminal operating expenses was offset to the tune of $4.2 million in annual Terminal revenues. (331 I. C. C. at 39, App. p. 126a) Appellants argument, in effect, is that they are entitled to the capitalized value of, for example, the revenues from power sold, which flow as income into the Terminal Account, unreduced by the cost of producing the power, which is included in the Terminal

expenses. Such a contention is not too far from the ultimate absurdity, which would have been that appellants are entitled to the capitalized value of the New Haven's passenger revenues, unreduced by the expenses of providing the passenger service, which exceeded the revenues, even with free use of the Terminal.

The Terminal operating expenses of about $9.5 million must obviously be reduced by the $4.2 million of Terminal income to arrive at a net figure of $5.3 million, of which the New Haven's 41-percent share would be about $2.17 million annually. That is the amount which has been offset by income from the hotels and office buildings. Capitalized at 8 percent, the $2.17 million would amount to about $27 million, instead of the $70 million figure used by appellants.

In any event, the Commission and the reviewing courts were clearly correct in holding that the New Haven's right to free use was worthless and that the New Haven is not entitled to the capitalized value of its share of the Terminal expenses.

In the decision of the three-judge statutory District Court dated July 10, 1968, Judge Friendly, writing for the majority, expressed serious doubt as to the New Haven's ability "to pass along its right to enter G. C. T. on what is now an expense-free basis despite the agreement's anti-assignment clause" and stated "there is no proof that this privilege would so increase the profitability of N. H.'s operations in New York State as to make them more valuable alive than dead." (289 F. Supp. at 431, App. p. 340a.)

The Reorganization Court on April 8, 1968, had appointed Judge John Van Voorhis as Special Master to hear and report respecting the New Haven's right, title or interest in the Grand Central Terminal properties. The Special Master filed his report on June 17, 1968, and a

supplemental report on July 22, 1968 (R. Doc. No. 59). In its memorandum of decision dated August 10, 1968, the Reorganization Court referred to the Special Master's report[1] as "a description of the nature of the legal interests of the New Haven in the G. C. T. properties, which this court accepts, adopts and incorporates by reference as a part of this opinion." (289 F. Supp. at 423, App. 252a) The Reorganization Court, however, "suggested that the Commission consider and make findings as to what value, if any, attaches to New Haven's present right to share in the income for the purpose of defraying its cost of operating in and out of the terminal," which was described as a "valuable interest." (289 F. Supp. at 463, App. p. 253a)

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[1] In his report of June 18, 1968, the Special Master stated (Spec. M. Rep. pp. 27-31, R. Doc. No. 59):

". . . I find the bondholders' contention to be untenable that New Haven has a complete undivided interest in the Grand Central Terminal non-operating properties, . . ."

* * *

"There can be no question that by mutual agreement these revenues from all of the Grand Central Terminal properties were pooled to apply on the fixed charges and maintenance and operational costs of the Terminal."

* * *

"It was not contemplated that if either railroad discontinued passenger trains into Grand Central the other would be saddled with the entire expense of a terminal larger than either railroad needed, without being credited with these entire revenues from the Grand Central Terminal properties to the extent that they were required to meet expenditures described in paragraph 14 and more specifically enumerated in paragraph 4."

* * *

"It should be borne in mind that under the construction which clearly should, as I think, be placed upon these agreements, the fixed charges upon land acquisition cost as well as the operational and maintenance expenses of the Terminal will continue to be paid out of the revenues entering the Terminal Account (even if New Haven passenger traffic were to be discontinued) in priority to the computation of any equity interest in the New Haven."

In remanding, both reviewing courts disapproved the original valuation of $13 million placed by the Commission on the New Haven's interest in the G. C. T. properties (331 I. C. C. at 684, App. p. 42a), which was increased by the Commission after remand to $28,887,000 in its fourth supplemental report, dated November 25, 1968. (334 I. C. C. at 39, App. 126a) In response to the Reorganization Court's request, the Commission found that station expenses "are a first charge on all terminal income"; that the New Haven's right to free use would have no value unless there was a buyer willing to pay for such use; and that no such buyer was in sight. (334 I. C. C. at 32, App. p. 119a)

In the memorandum of decision dated May 28, 1969, the Reorganziation Court adopted the Commission's disposition of the "free use" question[2] (App. pp. 294a-295a) Unfortunately, in a subsequent memorandum dated July 28, 1969, the Reorganization Court referred to the possibility that on appeal the "free use" right might be found to have a value, which could be as much as $70 million (App. pp. 314a-315a), and the appellants have placed great emphasis on this statement.

In its decision dated June 18, 1969, the District Court adhered to its previous view, stating (305 F. Supp. at 1060, App. p. 420a):

> "While we do not disagree with the bondholders' position that a state must pay the salvage value of

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[2] "After reading the briefs and hearing the arguments of all those who urged this point, and those opposed, the court is now satisfied that the Commission's treatment of the matter must stand. The Special Master and the Three Judge Court concluded there was no value in the interest, principally because it is not the kind of interest that would survive liquidation; nor, if it did, could it be assigned. . . . While mitigation of a burden may in some circumstances furnish a consideration, it is not a measurable one for the purpose of this issue in the case." (App. p. 294a)

property of a defunct railroad that it wishes to acquire, what is the 'salvage value' of property that cannot be sold to anyone else and is of no value in the owner's hands?"

In their briefs, Manufacturers (p. 59, footnote) and the Committee (pp. 128-129) refer to the fact that the States of New York and Connecticut have agreed with Penn Central to take over the former New Haven's commuter service between New Haven and New York City. They neglect to mention that the memorandum of intent, which was made public last November, generally contemplates an arrangement similar to that which formerly existed between the New Haven and Central. The States will, like New Haven, pay Harlem tolls for the use of the tracks between Woodlawn and G. C. T.; but they will *not* share in the expenses for taxes and interest on investment; and they will receive an annual credit of $2 million[3] from non-Terminal income toward their share of the *net* Terminal expense, which it is expected will give the States free use of the Terminal. Since the States will relieve Penn Central of a deficit operation and will spend many millions to modernize and rehabilitate the service, giving the States free use of the Terminal is a small price for Penn Central to pay in return. Since appellants have raised the matter of the agreement between the States and Penn Central, it is important to have the accurate facts in the record.

In summary, on the basis of an assumed liquidation, the New Haven's right to "free use" of the Terminal clearly has no value. It could not survive liquidation and, if it

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[3] As indicated above, the Terminal operating expenses were about $9.5 million and Terminal revenues about $4.2 million annually, so that New Haven's 41-percent share of the *net* Terminal operating expenses of $5.3 million was about $2.17 million. That figure, however, reflects the car and locomotive entrances of the New Haven's long-haul trains which the States will not take over, so that the $2 million annual credit should result in free use.

did, it could not be assigned. Tied in as it is to the performance of a deficit passenger service, it is more a liability than an asset. Penn Central will not be paid for transferring the "right" to the two States and should not be required to pay the New Haven estate anything for acquiring the "right."

CONCLUSION

For the foregoing reasons, the findings of the reviewing Courts that the New Haven's right to free use of Grand Central Terminal had no value which should be reflected in the purchase price, based on an assumed liquidation, should be affirmed.

Respectfully submitted,

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